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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 599

ANTHONY P. MILLER, INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 3a–41a) and the dissenting opinion (R. 41a–47a) are reported at 7 T. C. 729. The opinion of the Circuit Court of Appeals (R. 50–54) is reported at 164 F. 2d 268.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 18, 1947. (R. 55.) The petition for a writ of certiorari was filed on February 16, 1948. The jurisdiction of this Court is invoked under Section 240 (a) of the

Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether findings of fact of the Tax Court, supported by substantial evidence, were conclusive upon the appellate court.

STATUTES INVOLVED

The applicable statutes are printed in the Appendix, *infra,* pp. 15–17.

STATEMENT

The pertinent facts found by the Tax Court (R. 4a–18a) may be summarized as follows:

Compensation issue.—Anthony P. Miller is the president and controlling stockholder of the taxpayer corporation, which is engaged in the building and construction business in Atlantic City, New Jersey. (R. 4a.) Miller's duties as president were to obtain construction contracts and to plan, arrange for financing, design, and supervise construction projects. (R. 5a.)

In 1940 the taxpayer's operations were the largest in five years, the six construction projects in progress totaling over $3,000,000, as compared with a $2,000,000 contract in progress in 1936. The increased volume of operations in 1940 imposed an additional burden on Miller. In that year he obtained a loan of $400,000 for the taxpayer, and in connection therewith he and his

wife put up collateral worth $500,000. In 1940 Miller also spent considerable time in preparing and submitting estimates in connection with unsuccessful bids on approximately $25,000,000 worth of contracts. (R. 5a.)

During 1940 about 75% of the taxpayer's construction work in progress was being done by subcontractors. Miller acted as the taxpayer's general field superintendent and engineer in supervising the work of the subcontractors and was required to travel from project to project. In several instances it was necessary for the taxpayer to finish work which certain subcontractors were unable to accomplish because of financial difficulties. (R. 5a.)

Miller's supervisory activities kept him away from Atlantic City about five days a week. He kept in touch with his office by telephone and was required to do most of his office work at night and on weekends. His office staff consisted of a secretary, a bookkeeper, two clerks, and an engineer. Miller did not hire additional help for taxpayer as his experience in the past with field superintendents and engineers had been unsatisfactory. (R. 6a.)

In 1936 and 1937 Miller received $20,000 annually as compensation, half from the taxpayer and half from another corporation which was later merged into the taxpayer. (R. 4a, 6a.) In 1938, 1939, and 1941, the taxpayer paid him a

basic salary of $12,000 a year without bonus. For his services during 1940 he was allowed as compensation a basic salary of $12,000 and a bonus of $30,000. As controlling stockholder Miller determined the amount of salary and bonus he was to receive. (R. 6a.)

On these facts, the Tax Court without dissent found, as the Commissioner had determined, that the amount of $25,000 constitutes a reasonable allowance for compensation to Miller for his services to the taxpayer in 1940. (R. 7a.)

Chelsea stock issue.—After negotiations in 1938, the taxpayer agreed to furnish the necessary junior capital for a housing project in Atlantic City, and Irving Trust Company of New York (hereinafter referred to as "Irving") agreed to place a mortgage on the project, which was to be insured by Federal Housing Administration (hereinafter referred to as F. H. A.). Pursuant to the agreement, Irving gave a 28-year mortgage of $875,000, commencing May 1, 1939, with interest of 4½% per annum, payable August 1, 1939, and each quarter annually thereafter until November 1, 1940. Commencing February 1, 1941, payments of $14,218.75 representing both principal and interest were to be made quarterly. (R. 7a–8a.)

Also pursuant to the agreement the taxpayer organized the Chelsea Housing Corporation (hereinafter referred to as "Chelsea") to own and

operate the housing project, and furnished to it $100,000 in cash and land which had cost taxpayer $79,287.97, in return for 1,958 shares of Chelsea's no par common stock. (R. 8a–9a.)

The taxpayer was engaged to construct the project for $897,783 in cash and 390 shares of Chelsea no par common stock. It commenced construction in May, 1939, and expected to complete the project by October, 1939, but due to material shortages and weather, it did not finish it until July, 1940, and the stock was issued to it then. (R. 9a, 13a.)

The Chelsea project provided low rental apartments with a total of 261 family units. Because of the delay in completion, advantage could not be taken of the fall 1939 and spring 1940 rental seasons. Fifteen units were rented in March, 1940, and each month thereafter the number of units occupied increased until in July and August, 1941, 253 units were rented. In September and October, 1941, the occupied units decreased to 249 and 237, respectively. (R. 9a-10a.)

In 1940 rental conditions in Atlantic City were in general depressed. In June, 1940, Chelsea obtained permission from F. H. A. to reduce its rents, thus reducing its anticipated income by $9,870 per year. (R. 9a.) Due to this and the delay in completing the project, Chelsea's mortgage was in default early in 1940. Operating expenses were higher than expected, and in 1940

Chelsea was constantly behind in paying current expenses. It needed additional working funds but could obtain no further credit. Irving refused to modify the terms of the mortgage and rents could not be raised because of competitive reasons. (R. 10a.)

In these unfavorable circumstances, Miller as president of Chelsea and of the taxpayer considered abandoning the project. However, its rental manager persuaded him to continue and he, acting for the taxpayer, secured a $10,000 bank loan for Chelsea to meet the installment due on the mortgage in November, 1940. He also guaranteed Chelsea's accounts payable. In November, 1940, Chelsea was notified informally that it had been assessed for local tax purposes at a value of $850,000 as a basis for taxes to be levied in 1941. At the 1940 rate this indicated a 1941 tax of over $50,000. Although formal notice of the assessment would not be made until January, 1941, and the tax rate would not be fixed until July, 1941, the prospect in November, 1940, of a $50,000 tax expense in 1941, which was in excess of the anticipated tax expense of about $18,000, was unexpected and discouraging to the sponsors of the housing project. (R. 10a–11a.)

Acting for the taxpayer, Miller made further advances to the project in 1941, principally to meet current operating expenses. The rental manager had advised him to do so in order to

retain control until sufficient rentals had been received to recover these and prior advances. (R. 11a.)

On August 27, 1941, F. H. A. took possession and control of the project because of the continued mortgage defaults. F. H. A. appealed the local tax assessment made in November, 1940, and as a result reduced the 1941 local tax levy to about $30,000. On September 15, 1942, the mortgage was foreclosed, and Irving, the only bidder, purchased the property at a nominal price, conveying it pursuant to the mortgage-insurance contract to F. H. A. in return for F. H. A. bonds. In April, 1943, F. H. A. sold the project to agents of a new corporation for a price of $875,000, of which $30,000 was paid in cash and the balance was secured by a mortgage bearing 3% interest. (R. 11a–12a.)

Chelsea's balance sheet as of March 31, 1940, showed current asests of $46,200.11; current liabilities of $132,725.51; total assets of $1,058,-820.84; total liabilities of $894,620.84; and a net worth of $224,200. As of March 31, 1941, its balance sheet showed current assets of $11,922.78; current liabilities of $49,543.85; total assets of $1,130,098.97; total liabilities of $922,467.19; and net worth of $207,631.78. For the year ending March 31, 1941, it showed a net loss of $60,468.22. (R. 12a.)

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During 1940, in an effort to obtain money for financing construction projects, the taxpayer offered Chelsea stock as collateral. Several banks and agencies refused to accept such stock as security for a proposed loan. (R. 12a.)

On these facts the Tax Court found, as the Commissioner had determined, that the Chelsea stock did not become worthless in 1940, and that the taxpayer was not entitled to a deduction in 1940 in the amount of its cost of the stock owned by it. (R. 13a, 29a–34a.) The Tax Court also held that the value of the 390 shares of Chelsea stock received by the taxpayer on July 5, 1940, as partial payment for constructing the project was includible in its income, and it affirmed the Commissioner's determination that $39,000 was the value of this stock. (R. 13a, 34a–35a.) Five judges of the Tax Court dissented on the ground that under the evidence the 390 shares should be assigned a lesser value. (R. 45a–47a.)

Ogontz stock issue.—On August 24, 1940, the taxpayer received 449.6 shares of no par common stock of Ogontz Housing Corporation (hereinafter referred to as "Ogontz") in partial compensation for its services as general contractor in constructing an apartment project in Philadelphia, Pennsylvania. The project, containing 203 apartments, was completed in July, 1940, and for the fiscal year ending March 31, 1941,

Ogontz had a net loss of $51,015.58. The mortgage, which was insured by F. H. A., has been in default since the first payment was due but has not been foreclosed and Ogontz still has the project. (R. 14a, 16a.)

Pursuant to an agreement under which one George S. Idell accepted 350.4 shares of Ogontz no par common stock in partial payment for his services as architect, the taxpayer in 1939 received from Idell 116.4 shares of this stock in return for $8,270 in cash. During 1939 and 1940 Idell, without success, offered to sell other Ogontz shares at 25 cents on the dollar to various individuals, and he was also unable to sell the stock at any price through a broker specializing in unlisted securities. The stock of both Idell and the taxpayer was refused as collateral in 1940. (R. 14a–15a.)

On March 31, 1941, Ogontz's balance sheet showed current assets of $5,733.28; current liabilities of $42,807.89; total assets of $1,124,069.95; total liabilities of $909,985.53; and net worth of $214,084.42. (R. 15a.)

On these facts the Tax Court found that the 449.6 shares of Ogontz stock had a fair value of $71 a share when received by the taxpayer in 1940 and that the amount of $31,921.60, representing the value of the stock, was includible in taxpayer's income for 1940. (R. 17a, 35a–38a.)

Foster stock issue.—The taxpayer was general contractor in the construction of an apartment project owned by Foster Park Housing Corporation (hereinafter referred to as "Foster") and in partial payment for its services received, some time in 1940, 67.64 shares of Foster stock. On February 5, 1940, the taxpayer had paid $30,000 to Foster in return for 300 shares of its stock. The project was completed in December 1940, at which time tenants first began occupancy. (R. 17a.)

In 1940, one Morton Keast received 177.37 shares of Foster stock in partial payment for his services as architect. Keast included these shares in his 1940 income at a value of $7,480, which value has not been questioned by the Commissioner. In 1941 Keast obtained a bank loan, using the Foster stock as collateral. (R. 17a.)

On December 31, 1941, Foster's balance sheet showed current assets of $17,648.46; current liabilities of $967.27; and a net worth of $101,938.80. It had a net profit of $3,638.80 for 1941. (R. 17a.)

On these facts the Tax Court sustained the determination of the Commissioner that the Foster stock had a value of $100 per share in 1940 and was includible in taxpayer's income for 1940 in the amount of $6,764. (R. 18a, 38a–40a.)

The Circuit Court of Appeals affirmed the Tax Court's findings on each issue, since they were supported by substantial evidence. (R. 53–54.)

ARGUMENT

We submit that the petition in this case does not present a sufficient ground for the issuance of a writ of certiorari. The issues are all factual,[1] as the taxpayer agrees in its statement of the questions presented (Pet. 2), and the Circuit Court of Appeals affirmed for the reason that there are "abundantly sufficient facts to lend support to the Tax Court's conclusions". (R. 54). The full discussion of the conflicting evidence by the Tax Court (R. 29a–40a), considered with its findings of fact (R. 4a–18a), confirms that view. Indeed, the taxpayer does not now contend that any of the factual conclusions lack support in the evidence but argues only that the Circuit Court of Appeals took too restricted a view of its power of review. (Pet. 15–20.)

If it is assumed *arguendo* that the Administrative Procedure Act of 1946 applies to the Tax

[1] They are the validity of the Tax Court's findings that $25,000 is a reasonable allowance for compensation to taxpayer's president for his services in 1940 under Section 23 (a) (1) (A) of the Internal Revenue Code and Section 19.23(a)–6 of Treasury Regulations 103; that the Chelsea stock owned by taxpayer did not become worthless in 1940, so as to be deductible under Section 23 (g) of the Internal Revenue Code; and that the fair market values of the stocks received by the taxpayer as compensation for services in 1940, which are to be included in its income under Section 22 (a) of the Internal Revenue Code and Section 19.22(a)–3 of Treasury Regulations 103, are $100 per share for the Chelsea stock, $71 per share for the Ogontz stock, and $100 per share for the Foster stock.

Court,[2] as the taxpayer urges, the Circuit Court of Appeals was correct in this case, since Section 10 (e) (B) thereof (Appendix, *infra*) authorizes the reviewing court to reverse the findings and conclusions of an "agency", *inter alia,* when they are unsupported by substantial evidence. And

[2] In our view it does not. The Act applies only to "agency" actions, and Section 2 (a) (Appendix, *infra*) excludes "the courts" from the definition of "agency". While the Tax Court technically is an independent agency in the executive branch of the Government (*Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716; *Commissioner* v. *Gooch Milling Co.*, 320 U. S. 418, 420), Congress had already enacted statutes governing its authority, the conduct of its proceedings, and review of its decisions. Sections 1100–1121 and 1141–1142 of the Internal Revenue Code. It seems unreasonable to suppose that Congress intended by the new Administrative Procedure Act, dealing with "agency" actions generally, to rescind its earlier legislation dealing explicitly with the Tax Court, without expressly disclosing that intent. When the Act was pending before Congress, in response to an inquiry from the Chairman of the Judiciary Committee of the Senate, the Attorney General advised by letter that the proposed Act would not apply to the Tax Court, and the Senate Committee appended this letter to its report. Appendix B to S. Rep. No. 752, 79th Cong., 1st Sess., p. 37, *et seq.* (S. Doc. 248, 79th Cong., 2d Sess., pp. 223–231). Nothing in the legislative history indicates that Congress did not share this understanding. The dictum in *Lincoln Electric Co.* v. *Commissioner*, 162 F. 2d 379, 382 (C. C. A. 6th), that the power of the court to review Tax Court decisions "doubtless has been broadened" by the Administrative Procedure Act seems inconsistent with the same court's decision in *Commissioner* v. *Wiesler*, 161 F. 2d 997 (C. C. A. 6th), rendered at almost the same time. Furthermore, the dictum in the *Lincoln Electric Co.* case was disapproved in *Anderson* v. *Commissioner*, 164 F. 2d 870, 874 (C. C. A. 7th).

under Section 1141 (c) of the Internal Revenue Code (Appendix, *infra*), authorizing a reviewing court to reverse a decision of the Tax Court if it is "not in accordance with law", the "substantial evidence" rule has always consistently been employed as the standard for review of factual findings of the Tax Court, both before and after the decision in *Dobson* v. *Commissioner,* 320 U. S. 489, rehearing denied, 321 U. S. 231. E. g., *Elmhurst Cemetery Co.* v. *Commissioner,* 300 U. S. 37; *Wilmington Co.* v. *Helvering,* 316 U. S. 164; *Commissioner* v. *Scottish American Co.,* 323 U. S. 119; *Boehm* v. *Commissioner,* 326 U. S. 287, rehearing denied, 326 U. S. 811. Thus, the Circuit Court of Appeals applied the correct standard of appellate review of factual findings under both statutes. Cf. *Credit Bureau of Greater N. Y.* v. *Commissioner,* 162 F. 2d 7, 9 (C. C. A. 2d); *Anderson* v. *Commissioner,* 164 F. 2d 870, 874 (C. C. A. 7th). Consequently, in this case there is no necessity for this Court to consider whether the Administrative Procedure Act applies to the Tax Court, as the dictum in *Lincoln Electric Co.* v. *Commissioner,* 162 F. 2d 379, 392, suggests (Pet. 15–17), or to reconsider the principles stated in *Dobson* v. *Commissioner, supra* (Pet. 18–20).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MARCH, 1948.

APPENDIX

Administrative Procedure Act, c. 324, 60 Stat. 237:

DEFINITIONS

SEC. 2. As used in this Act—

(a) *Agency.*—"Agency" means each authority (whether or not within or subject to review by another agency) of the Government of the United States other than Congress, the courts, or the governments of the possessions, Territories, or the District of Columbia. Nothing in this Act shall be construed to repeal delegations of authority as provided by law. * * *

* * * * *

JUDICIAL REVIEW

SEC. 10. Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—

* * * * *

(e) *Scope of review.*—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or other-

wise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

Internal Revenue Code:

SEC. 1141. COURTS OF REVIEW.

(a) *Jurisdiction.*—The Circuit Court of Appeals and the United States Court of Appeals for the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board, except as provided in section 239 of the Judicial Code, as amended, 43 Stat. 938 (U. S. C. Title 28, § 346); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended, 43 Stat. 938 (U. S. C., Title 28, § 347).

* * * * *

(c) *Powers.*—

(1) *To affirm, modify, or reverse.*—Upon such review, such courts shall have

power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.

* * * * *

(26 U. S. C. 1940 ed., Sec. 1141.)

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